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No. 99-1235

IN THE

Supreme Court of the United States

GREEN TREE FINANCIAL CORP. -- ALABAMA,
AND GREEN TREE FINANCIAL CORPORATION,
Petitioners,

v.

LARKETTA RANDOLPH,
Respondent.

On Writ of Certiorari to the United States
Court of Appeals for the Eleventh Circuit

BRIEF *AMICUS CURIAE* OF PUBLIC CITIZEN IN SUPPORT OF RESPONDENT

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INTEREST OF THE AMICUS[1]

Public Citizen is a national consumer organization with approximately 150,000 members. While Public Citizen recognizes the appropriate role that consensual arbitration plays, it has a longstanding interest in preventing large institutions from compelling consumers and workers to forgo their rights to proceed in court, especially where, as here, arbitration does not merely involve a change in forum, but also affects a significant reduction in remedies and other rights, either as a matter of law or, as here, as a matter of practical necessity. In addition, the rights of the thousands of absent members of the class that respondent sought to maintain in this action will be effectively determined by whether the decision of the Eleventh Circuit is upheld. Because Public Citizen regularly participates in class actions to protect the interests of absent class members, its brief here will focus on their interests in having the decision below affirmed.

Amicus agrees with the arguments made in respondent's brief, and they will not be repeated here. Instead, amicus will provide a detailed history of the Federal Arbitration Act of 1925 to establish that the Act was not intended to be an unqualified endorsement of arbitration under all circumstances, but a more limited approval of consensual agreements between businesses to arbitrate their differences, without altering the substantive rights of either party. In this case, compelled arbitration of the Truth in Lending Act claims of respondent

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[1] Letters of consent to the filing of this *amicus* brief have been lodged with the Clerk. Pursuant to this Court's Rule 37.6, *amicus* states that no party had any role in writing this brief and that no one other than *amicus* or its counsel made a monetary contribution to its preparation or submission.

and the class that she seeks to represent would effectively foreclose the exercise of their rights because of the costs that claimants would have to incur in pursuing arbitration and because of the absence of class action remedies that are essential to TILA enforcement. Thus, compelling arbitration here would not further the purposes of the FAA and would undermine the purposes of TILA, as the Eleventh Circuit correctly held.

Finally, although we agree with respondent that the decision below should be affirmed, we do not support her suggestion that, if the agreement at issue here had somehow specifically authorized class arbitration, that would have cured this defect. In our view, only an instrumentality of government, and not a private arbitrator, can issue orders that can bind absent class members. In taking this position, amicus provides a perspective entirely different from those of the parties.

INTRODUCTION AND SUMMARY OF ARGUMENT

This case involves a claim brought by a mobile-home purchaser against her mortgage company on behalf of herself and a proposed class of borrowers under the Truth In Lending Act's express class action provisions. Respondent's complaint sought class certification and appropriate class-wide relief for petitioner's failure to inform consumers that its financing documents required them to purchase a $15 vendors' single-interest insurance policy. In its contracts with each class member, petitioner included an extremely broad and identical arbitration provision that requires borrowers to arbitrate all contractual and statutory claims for both damages and injunctions. The contract does nothing to change the general rule that the parties to an arbitration must share forum costs, such as the fees of the decision-maker, unlike in court proceedings where judges are paid by the government.

Moreover, despite the breadth of the arbitration clause, it makes no mention of class actions and plainly does not contemplate that a private arbitrator would have the power, let alone the tools, to adjudicate these claims on a class-wide basis.

Although the District Court recognized that requiring arbitration here would almost certainly end this proceeding, it concluded that it had no choice but to order arbitration and to dismiss the case with prejudice, a ruling to which it adhered on respondent's motion for reconsideration. The Court of Appeals reversed, concluding that it had jurisdiction over a final decision of dismissal and finding that the failure to shift the burden of the expenses of arbitration to petitioner fundamentally interfered with respondent's enforcement of TILA in these circumstances.

Amicus agrees with respondent that the Court of Appeals had jurisdiction over her appeal. Section 1291 of Title 28 provides for jurisdiction over "final decisions"of district courts, and Section 16(a)(3) of the FAA confirms that authority using identical terminology, with no qualifications whatsoever. Petitioner never explains what else remains to be done to make the decision final, nor when else a person who declines to arbitrate, as respondent did here, could take an "appeal" from this order of dismissal, let alone how a person who prevails in arbitration can "appeal" a victory in that forum, when the real objection is to the defeat in the judicial forum that occurred well in the past. Finally, of particular interest to amicus, what would happen to the claims of absent class members while the case was wending its way through arbitration, and, in particular, would their statutes of limitations be tolled until somehow the class representative was able to appeal the final decision of dismissal? All of those problems can be avoided by reading "final decision" in Section 16(a)(3) to mean what it has always meant: A losing party may take an appeal whenever, as

here, there is nothing left to be done in the District Court.

Contrary to the assertions by petitioner and its amici, the FAA was never intended to be a paean to arbitration to the exclusion of all other interests. The history of the FAA makes clear that it was enacted in response to the refusal of courts to enforce arbitration agreements and even arbitration awards between businesses. Congress recognized other values in the Act and never contemplated that statutory claims, which depend on the courts for meaningful enforcement, would be undermined by the kind of pre-dispute arbitration clauses inserted by petitioner here in all of its contracts. It is not our position that statutory claims are never a proper subject of arbitration, but that the history of the Act confirms this Court's recognition in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 637 (1985), that arbitration clauses cannot undermine the effective enforcement of substantive rights, particularly those under laws like TILA that are intended to override ordinary principles of contract law.

That approach is of particular significance here, where the class action device has been recognized by Congress as vital to TILA enforcement. As respondent demonstrates, the absence of a class action mechanism, as well as the lack of a requirement that petitioner bear the cost of arbitration, makes these TILA claims effectively unenforceable if she must proceed in arbitration. But even if petitioner agreed to pay for arbitration costs and purported to create a class action arbitration forum, that would be of no avail. Consistent with due process, a non-party can lose his or her claim only by governmental action, not by a private arbitration. Thus, absent class members have the right to the protection of a court before their claims are adjudicated, and only a unit of government, not a private party like petitioner, can create such a forum. This Court need not pass on the legality of such a hypothetical

private class action mechanism, but the obvious and serious problems with the concept provide a further reason to conclude that a court, not an arbitrator, must pass on the merits of these statutory claims.

ARGUMENT

The decision of the Court of Appeals below should be affirmed.

I. Congress Never Intended the Federal Arbitration Act to Allow a Party Effectively to Extinguish Opposing Legal Claims by Imposing Prohibitive Arbitration Costs on Their Enforcement.

Petitioner attempts to answer the questions presented in this case primarily by reference to an "emphatic" federal policy favoring arbitration. In arguing that the Federal Arbitration Act's express provision for the appeal of a "final decision with respect to an arbitration that is subject to this title," 9 U.S.C. § 16(a)(3), does not apply to the district court's decision dismissing all of respondent's claims with prejudice, petitioner relies foremost on the FAA's "object and policy" favoring arbitration. Br. at 21. Asserting that its arbitration clause should be enforced despite its threat to impose hundreds of dollars in additional forum costs on consumers seeking to enforce their $200 Truth In Lending Act claims, petitioner recites the enforcement language of Section 2 of the FAA, Br. at 31, on the assumption that it applies to all arbitration agreements, no matter what the subject or how the agreement affects substantive rights.

The history of the FAA, however, provides no support for petitioner's invocation of a boundless federal policy

favoring arbitration of all disputes between contracting parties. The events leading to the FAA's passage demonstrate a prevailing consensus that arbitration was an expeditious and cost-effective mechanism for resolving business contract disputes. Although this Court has subsequently recognized broader applications of the Act to statutory claims, *Mitsubishi*, 473 U.S. at 626-27; *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26 (1991), and to disputes arising from consumer transactions, *Allied-Bruce Terminix Companies, Inc. v. Dobson*, 513 U.S. 265 (1995), the Court has also been careful to ensure that arbitration continues to serve the Act's dual goals of allowing for faster and cheaper resolution procedures, while preserving all of a party's legal remedies. *See, e.g., Mitsubishi*, 473 U.S. at 628:

> By agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits their resolution in an arbitral, rather than a judicial, forum. It trades the procedures and opportunity for review of the courtroom for the simplicity, informality, and expedition of arbitration.

Petitioner's use of arbitration in this case threatens plaintiffs with arbitration-specific costs that would prevent them from vindicating their rights under the Truth In Lending Act. This use of mandatory arbitration would exceed the bounds set by the FAA's underlying policy goals and thus requires the Court to reassert the limitations set by Congress on the FAA's enforcement.

The history of the Federal Arbitration Act defines the contours of federal policy regarding arbitration. While Section 2 speaks generally to enforcement of a "contract evidencing a transaction in interstate commerce," for the settlement of a

"controversy thereafter arising out of such contract," 9 U.S.C. § 2, the process culminating in the FAA's passage in 1925 makes clear the circumstances in which the Act provides for the enforcement of arbitration. This history reveals more than isolated statements as to the Act's likely application; it demonstrates an overwhelming consensus among legislators, drafters and supporters, as confirmed by the then-prevailing state law, that arbitration was to be used to provide a faster and cheaper method for resolving contractual disputes between businesses. On proper uses of legislative history, *compare Tennessee Valley Authority v. Hill*, 437 U.S. 153, 177 (1978) ("The legislative proceedings in 1973 are, in fact, replete with expressions of concern over the risk that might lie in the loss of *any* endangered species"), *with Securities and Exchange Comm'n v. Sloan*, 436 U.S. 103, 121 (1978) ("We are extremely hesitant to presume general congressional awareness...based only upon a few isolated statements in the thousands of pages of legislative documents"). As we now show, petitioner's attempt to use arbitration to create barriers to plaintiffs' assertion of statutory claims is wholly unjustified by reference to the FAA's history and purposes.

Congress enacted the Federal Arbitration Act in 1925 to allow businesses to resolve their contractual disputes before experienced decision-makers in expedited, cost-effective proceedings. The FAA was the legislative culmination of a process that the American Bar Association set into motion to obtain congressional authorization for federal courts to enforce arbitration agreements in maritime and interstate commercial contracts. *See* Joint Hearings on S. 1005 and R. 646 before the Subcommittees of the Judiciary Committees (Joint Hearings), 68th Cong., 1st Sess. 34 (1924). The ABA's Committee on Commerce, Trade, and Commercial Law described its legislative proposal thus:

> [T]he adoption of ...the Federal statute and the uniform State statute will put the United States in the forefront in this procedural reform. It will raise the standards of commercial ethics. It will reduce litigation. It will enable business men to settle their disputes expeditiously and economically, and will reduce the congestion in the Federal and State courts.

Hearing on S. 4213 and S. 4214 before the Subcommittee of the Senate Committee on the Judiciary, 67th Cong., 4th Sess. (Senate Subcommittee Hearing) 14 (1923). The ABA's legislative proposal was intended to provide merchants with faster and cheaper procedures for resolving commercial contract disputes, and was not intended to establish a general federal policy favoring arbitration of all controversies between contracting parties. *See* Report of Standing Committee on Commerce, Trade and Commercial Law, 50 ABA Rep. 356, 361 (1925) (arbitration's "appropriate field in respect to future disputes is somewhat qualified and limited. It is, in our opinion, desirable that this Association should lend its influence and aid to arbitration within its proper field.") (quoting committee study of Association of the Bar of the City of New York).

The ABA drafted the proposed federal arbitration law in response to problems experienced primarily by commercial actors. In addition to the costs of litigation, the ABA drafters were concerned with delays that the litigation process entailed, "especially in recent years in centers of commercial activity, where there has arisen great congestion of the court calendars," and with the

> failure, through litigation, to reach a decision regarded as just when measured by the

> standards of the business world. This failure may result either because the courts necessarily apply general rules which do not always fit a specific case, and [sic] because, in the ordinary jury trial, the parties do not have the benefit of the judgment of persons familiar with the peculiarities of the given controversy.

Joint Hearings 34-35 (ABA Brief on proposed Federal arbitration statute). These limited purposes should signal caution whenever the Act is invoked outside the context of business contract disputes. Statutory claims compel decision-makers to apply special rules designed to vindicate legislatively-declared public values, which exist wholly apart from, and often in conflict with, commercial norms. The Truth In Lending Act, for example, supersedes general principles of contract law, requiring decision-makers to enforce the Act's remedies to vindicate consumer protection goals. This is an entirely different function from that which the FAA's architects expected arbitrators to perform.

During congressional hearings on the bills that were later enacted as the FAA, the ABA drafters supported their legislative proposal by reference to its impact on merchants. W.H.H. Platt, chair of the ABA's commerce committee, explained to the Senate Judiciary subcommittee that the legislation responded to "quite a demand in commercial centers on the part of a good many commercial organizations to have...a vehicle constructed to effectuate an agreement to arbitrate." Senate Subcommittee Hearing 8. Julius H. Cohen, also of the ABA commerce committee, explained that federal courts "could get rid of the litigation that these business concerns can prevent by their arbitration committees" because the Act "would take out all these matters of business and leave the courts free to handle the business that ought to be handled

with dispatch." Joint Hearings 18; *see also* J.H. Cohen and K. Dayton, *The New Federal Arbitration Law*, 12 Va. L. Rev. 265, 281 (1926):

> Not all questions arising out of contracts ought to be arbitrated. It is a remedy peculiarly suited to the disposition of the ordinary disputes between merchants as to questions of fact—quantity, quality, time of delivery, compliance with terms of payment, excuses for non-performance, and the like. It has a place also in the determination of the simpler questions of law—the questions of law which arise out of these daily relations between merchants as to the passage of title, the existence of warranties, or the questions of law which are complementary to the questions of fact which we have just mentioned. It is not the proper method for deciding points of law of major importance involving constitutional questions or policy in the application of statutes.

The FAA was enacted with the intention that the Act would not subvert legal remedies because arbitration would be enforced only where it could provide a full and fair resolution to a dispute involving private interests.

Commercial sector supporters likewise viewed the FAA in terms of its application to contractual disputes between businesses. Charles Bernheimer of the New York Chamber of Commerce was unambiguous in expressing his understanding of this limited application of arbitration legislation:

> There are four known methods based on long experience I have had by which to meet trade

> disputes, *the ordinary everyday trade disputes, and it is for them that this legislation is proposed...*
>
> Speaking for those who have had experience and who are engaged in business, I may say this, that arbitration saves time, saves trouble, saves money. There is no question about that. We know it. *It preserves business friendships. ...Friendliness is preserved in business. It raises business standards.*

Joint Hearings 7 (emphasis added). Other supporters echoed this understanding. *Id.* at 11-12 (Gray Silver of the American Farm Bureau Federation: "we are very much in favor of the objectives of an arbitration in commercial matters, believing it will be helpful in speeding business generally"); *Id.* at 22 (M.L. Toulme of the National Wholesale Grocers' Association: "This association for many years has urged commercial arbitration"); *Id.* at 23 (Thomas Paton of American Bankers' Association: endorsing legislation "legalizing the settlement of commercial disputes"); *Id.* at 23-24 (Samuel Forbes of the Converters' Association: "we most strongly feel that the adoption of a Federal arbitration act such as is now proposed will be one of the most forward steps in commercial life. Our members have found arbitration to be expeditious, economical, and equitable, conserving business friendships and energy").

The views of the American Bankers' Association, a vocal supporter of federal arbitration legislation in the early 1920's, are also instructive regarding the disconnect between the FAA's statement of federal arbitration policy and the home mortgage borrowers' statutory claims that form the basis of the dispute here. The bankers passed the following resolution in 1923 supporting the federal bill:

> Whereas all merchants doing interstate and foreign business seek a method whereby disputes arising in their daily business transactions can be speedily, economically, and equitably disposed of; and
> Whereas arbitration offers the best means yet devised for an efficient, expeditious, and inexpensive adjustment of such disputes;
> Whereas the arbitration laws of the various States of the Union are not in uniformity and often in conflict; and
> Whereas the laws of any given State are not applicable in other States: Now therefore be it
> *Resolved.* That the commerce and marine commission of the American Bankers' Association is thoroughly in accord with the efforts being made to create Federal legislation legalizing the settlement of commercial disputes...

Id. at 31. The bankers' representative during the 1924 Joint Committee Hearings responded to the question of how banks stood to benefit from the Act solely by reference to business disputes:

> I think [the federal legislation] would be of indirect benefit, because [the bankers'] interests are linked up with the merchants and business men of the country; and later on it will probably be of direct benefit to the banks because it will put in their minds the idea of taking up their disputes through arbitration. Of course, the banks of the country have a great deal of business, and a great many business dealings with one another throughout the country in

> regard to bank collections, and there is a great deal of conflict in regard to those bank collections. I think this would be the best method of handling that litigation.

Id. The banking representatives were silent about any benefits of the Act's application to compel arbitration of statutory claims asserted by non-commercial account holders or borrowers because they, like other supporters, expected the FAA to have a narrow application to business relationships.

Prevailing arbitration law at the time of the FAA's enactment further illustrates the limited range of federal arbitration policy. The FAA's supporters repeatedly compared the federal arbitration legislation to existing state laws, particularly the New York Arbitration Law, which permitted courts to enforce agreements to arbitrate commercial disputes. The federal act was meant to parallel New York's, but would apply to maritime and interstate and foreign commercial transactions that were then deemed beyond the reach of state law. S. Rep. No. 536, 68th Cong., 1st Sess., 3 (1924); Senate Subcommittee Hearing at 2; Joint Hearings at 8, 16, 19, 24, 30, 34. The New York Arbitration Law enforced agreements to arbitrate disputes arising out of commercial contracts. Julius Cohen of the ABA's commerce committee described the public policy behind the New York statute as one of providing a "strong inducement toward adjusting trade difficulties out of court and thus preserving the good relations between the parties, while securing a fair and reasonable adjustment of the controversy at hand." Julius Henry Cohen, *The Law of Commercial Arbitration and the New York Statute*, 31 Yale L. J. 147, 152 (1921). Congress's understanding of the FAA at the time of its enactment was that it would apply to enforce agreements negotiated between businesses to resolve their contractual disputes.

When courts unleash the FAA from its originally intended context of contractual disputes between businesses and apply it to compel arbitration of consumer's statutory claims, they must ensure that arbitration preserves all of the consumer's legal rights. This capacity of arbitration cannot simply be presumed because consumers, unlike businesses, typically do not negotiate contractual terms, but rather accept contracts, including those with arbitration clauses, on a take-it-or-leave-it basis, have less experience and knowledge of arbitration than do the businesses against whom they assert their claims, and lack the capacity of businesses to monitor arbitral proceedings on an ongoing basis. *See*, *Cole v. Burns Int'l Security Services*, 105 F.3d 1465, 1476-77 (D.C. Cir. 1997) (discussing disadvantages of individual workers in arbitration against employers). The power and experiential disadvantages of consumers in arbitration leave them vulnerable to burdens that businesses may place on their ability to enforce their legal rights. The silence of petitioner's contract as to arbitration costs, for example, requires respondent and other mortgage borrowers to face a risk of additional costs not payable in a court adjudication that may prohibit them from ever enforcing their statutory rights because their costs may exceed their expected recovery. Because Congress never intended or anticipated applications of the FAA that would create these dangers, courts cannot compel consumer arbitration by presuming the existence of consensual arrangements and fair procedures that preserve all of the consumer's legal claims. Instead, the party seeking to compel arbitration must demonstrate that these preconditions to arbitration have been satisfied.

The discussion during Congressional hearings of what federal arbitration legislation was *not* expected to cover confirms that federal arbitration policy in the FAA does not extend to petitioner's contract. In response to questions from

Senate Judiciary subcommittee Chairman Sterling and from Senator Walsh expressing concern about unequal bargaining power and compelled waivers of the right to litigate, the ABA drafters repeatedly proclaimed that the Act would not apply to insurance contracts. Senate Subcommittee Hearing at 9, 10; Joint Hearings at 15. When pressed by Senator Walsh, ABA representative W.H.H. Platt also disavowed the applicability of the proposed legislation to railroad passenger agreements because of the comparability of arbitration in these cases to prohibited contractual barriers to litigation, such as coerced reductions of statutes of limitations. Senate Subcommittee Hearing at 10 ("I think that ought to be protested against, because it is the primary end of this contract that it is a contract between merchants one with another, buying and selling goods"). The legislators' concern to avoid compelled waivers of legal rights, and the drafters' responses distinguishing contracts between parties of unequal bargaining power from the commercial contracts they sought to cover, confirm that the Act may not be used to alter substantive rights, as petitioner would do here if it prevails.

The FAA's exclusion of employment contracts from its coverage also bolsters the conclusion that the federal policy regarding arbitration is far narrower than petitioner asserts. As the bill was first proposed in the Senate in 1922, Section 2 was silent as to employment contracts, S. 4214, 67th Cong. § 2 (1922). When Committee Chairman Sterling questioned the ABA's Platt as to this possible application during the 1923 Senate hearings, Platt disavowed any intent to apply the proposed law to employment relationships:

> It was not the intention of this bill to make an industrial arbitration in any sense; and so I suggest that in as far as the committee is concerned, if your honorable committee should

> feel that there is any danger of that, they should add to the bill the following language, "but nothing herein contained shall apply to seamen or any class of workers in interstate or foreign commerce." It is not intended that this shall be an act referring to labor disputes at all. *It is purely an act to give the merchants the right or the privilege of sitting down and agreeing with each other as to what their damages are, if they want to do it. Now, that is all there is in this.*

Senate Subcommittee Hearing at 9 (emphasis added); *see also Id.* at 14 (Statement of Secretary of Commerce Herbert Hoover, proposing identical statutory language). In response to these proposals, Congress amended Section 1, adopting this exclusionary language to clarify the Act's non-application to employment agreements and its limited application to contracts between businesses. The purpose of Section 1's exclusionary clause—to distinguish employment from commercial contracts—also counsels this Court to proceed carefully when applying the FAA to contracts purporting to bind individuals to arbitrate their statutory disputes with businesses.[2]

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[2] This Court has granted certiorari in *Circuit City Stores, Inc. v. Adams*, 99-1379, to determine the scope of the FAA's Section 1 exclusion of employment contracts. Amicus respectfully urges that the entire discussion of the FAA's enactment herein, not merely that of Section 1, informs the correct disposition of *Adams*. Courts that have narrowed Section 1's exclusion have ignored altogether Congress's work in enacting the FAA. *See, e.g., Cole*, 105 F.3d at 1470; (deeming § 1's legislative history irrelevant to its application); *O'Neil v. Hilton Head Hosp.*, 15 F.3d 272, 274 (4th Cir. 1997). Under prevailing Commerce Clause doctrine in 1925, *see, e.g.*,

Supporters of the FAA's enactment also were unanimous in their expectation that the Act would reduce the time and expense of resolving the disputes to which the Act would apply. The House and Senate Judiciary Committees identified the delays and costs of litigation as a major impetus for federal legislation authorizing arbitration of certain disputes. H.R. Rep. No. 96, 68th Cong., 1st Sess., 2 (1924); S. Rep. No. 536, 68th Cong., 1st Sess., 3 (1924). In urging passage of the legislation, the Commerce Department pointed the Committees' attention to federal court "delays amount[ing] to a virtual denial of justice." Senate Hearing at 14. The ABA's brief in support of its legislative proposal recited as one of the bill's primary benefits that it would "enable business men to settle their disputes expeditiously and economically and will reduce the congestion in the Federal and State courts." *Id.* Charles Bernheimer of the New York Chamber of Commerce concurred, informing the Joint Committees that "arbitration saves time, saves trouble, saves money." Joint Hearings at 7.

Petitioner's use of arbitration to impose forum costs on consumers vindicating statutory claims is wholly at odds with federal arbitration policy under the FAA. In order to arbitrate her statutory claim, respondent faces the threat of filing fees and arbitrator's fees, which may be in the hundreds of dollars per day, plus additional forum expenses. These costs

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United Leather Workers Int'l Union v. Herkert & Meisel Trunk Co., 265 U.S. 455, 465 (1924) ("'The making of goods and the mining of coal are not commerce, nor does the fact that these things are to be afterwards shipped or used in interstate commerce make their production a part thereof.'") (citations omitted), the exclusion of "seamen, railroad employees, or...any workers engaged in foreign or interstate commerce," 9 U.S.C. § 1, was tantamount to an exclusion of all workers.

effectively prohibit consumers with small claims, like respondent's $200 cause of action, from enforcing their legal rights in arbitration. To preserve the FAA's guarantee that parties may vindicate all of their legal claims, the drafter of a contract that would compel consumers to arbitrate must bear all of the costs associated with the forum, including filing fees, arbitrator's fees, and other hearings costs, that exceed the equivalent costs to litigants in court. At the very least, consumers who prevail in arbitration must be guaranteed to recover these costs plus all those provided for under 28 U.S.C. § 1920, or its state law equivalent if the case were pending in state court.[3]

The legislative history of the Federal Arbitration Act demonstrates that the Act may not be invoked to compel consumers to arbitrate statutory claims at a cost exceeding that of the equivalent judicial forum. While the Act's original application to contractual disputes between businesses has been expanded in recent years, this Court has ensured that arbitration continues to serve the underlying purposes of the Act to preserve parties' legal claims while allowing them to resolve those claims in timely and cost-effective proceedings. Petitioner's use of arbitration in this case, to threaten individual consumers with forum-specific costs as the price for asserting their statutory claims, would undermine the policy goals of the FAA and therefore the Court may not compel borrowers to arbitrate these Truth In Lending Act claims.

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[3] Respondent's Truth In Lending Act claims could also have been filed in state courts under 15 U.S.C. § 1640(c). Since this would open up small claims courts to TILA claimants, the availability of a low cost judicial forum in this case makes the deterrent effect of petitioner's shifting of arbitral forum costs to consumers that much more pronounced.

II. The Truth In Lending Act's explicit class action remedies, which are essential to its consumer protection goals, cannot be enforced through arbitration.

Enforcement of the arbitration clause in petitioner's retail installment contract would prohibit respondent and other home mortgage borrowers from vindicating their rights to seek class-wide relief under the Truth In Lending Act. Petitioner does not dispute the contention that its arbitration clause precludes borrowers from proceeding against it as a class, but instead asserts that individual remedies are sufficient to enforce TILA. Brief at 46-47. However, TILA's class action remedies constitute a critical component of the Act's civil enforcement scheme. Because there can be no mandatory arbitration of the claims of a nationwide plaintiff class, petitioner's arbitration clause eliminates class relief under TILA and therefore is unenforceable.

A. The Truth In Lending Act's class action remedies are essential to the effective enforcement of the Act against repeat violators.

Contractual arbitration clauses that prevent prospective litigants from effectively vindicating statutory causes of action are unenforceable. *Mitsubishi*, 473 U.S. at 637; *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 227 (1987). In *Mitsubishi*, the Court enforced an arbitration agreement between an automobile manufacturer and a distributor as it applied to the distributor's Sherman Act counterclaims. The Court did so because the arbitration tribunal was bound to apply the Sherman Act's remedial provisions, concluding that "so long as the prospective litigant

may vindicate its statutory cause of action in the arbitral forum, the statute will continue to serve both its remedial and deterrent function." *Mitsubishi*, 473 U.S. at 637. Under this analysis, however, petitioner may not compel arbitration of respondent's Truth In Lending Act claim because arbitration will deny respondent TILA's class action remedies.

The potential for class action liability is essential to the effective enforcement of the Truth In Lending Act. TILA requires lender institutions to disclose to borrowers all credit terms and costs associated with a particular consumer loan. 15 U.S.C. § 1601(a). Civil litigation is the primary and preferred means chosen by Congress for the enforcement of TILA requirements. Sen. Rep. No. 93-278, at 14 ("[t]he purpose of the civil penalties section under Truth in Lending was to provide creditors with a meaningful incentive to comply with the law without relying upon an extensive new bureaucracy"); *see also Watkins v. Simmons & Clark, Inc.*, 618 F.2d 398, 400 (6th Cir. 1980) ("Congress felt constrained to encourage class actions in the truth-in-lending context because of the apparent inadequacy of the Federal Trade Commission's enforcement resources and because of a continuing problem of minimal voluntary compliance with the Act on the part of creditors"). Since many TILA violations involve a lender's failure to disclose a finance charge whose cost to consumers is relatively low, borrowers suing to enforce the Act bear the risk, if unsuccessful, of having to incur expenses far in excess of the value of their individual statutory claims. See 15 U.S.C. § 1640(a) (limiting recovery for individual claimants to actual damages or $200 to $2,000 in statutory damages, plus attorney fees and costs). These costs of mandatory individual proceedings would pose an effective bar to TILA enforcement.

This Court has recognized repeatedly that class actions are necessary to preserve causes of action where individual

claims are of relatively small value:

> The aggregation of individual claims in the context of a class-wide suit is an evolutionary response to the existence of injuries unremedied by the regulatory action of government. Where it is not economically feasible to obtain relief within the traditional framework of a multiplicity of small individual suits for damages, aggrieved persons may be without any effective redress unless they may employ the class action device.

Deposit Guaranty Nat'l Bank v. Roper, 446 U.S. 326, 339 (1980); *see also Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 161 (1974); *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 809 (1985). The TILA's class action remedies even out the incentives by authorizing class recoveries of up to $500,000 plus costs and attorney fees, 15 U.S.C. § 1640(a)(2)(B), and simultaneously encourage voluntary compliance with the Act through the threat of these substantial enforcement penalties.

Congress adopted the TILA class action remedies to ensure effective civil enforcement while protecting violators of the Act from the threat of insolvency. The 1974 amendments represent a congressional response to courts' refusal to certify TILA plaintiff classes because, if each member recovered the statutory minimum, the aggregate recovery might render the lender insolvent. Sen. Rep. No. 93-278 at 14. By expressly authorizing TILA class actions, but capping class recoveries, Congress rejected the finance industry's defense of the judicial status quo and adopted the Federal Reserve Board's position that "potential class action liability is an important encouragement to the voluntary compliance which is so necessary to insure nationwide adherence to uniform

disclosure." *Id.* at 15 (quoting Federal Reserve Board opinion). When Congress later amended Section 1640 to raise the class recovery ceiling to $500,000, it reiterated that private litigation was the Act's chief enforcement tool, that the statutory cap on class recoveries was not meant to discourage class actions, and that any impediment to class proceedings would "frustrate[] the enforcement policy for which class actions are recognized." Sen. Rep. No. 94-590, at 438; *see also Watkins*, 618 F.2d at 402 ("the legislative history surrounding these amendments convinces us that Congress did intend, by them, to encourage class actions and to use the threat of class action recoveries to force compliance with the Act"); *Johnson v. Tele-Cash, Inc.*, 82 F. Supp.2d 264, 270 (D. Del. 1999) (holding short-term loan dealer's arbitration clause unenforceable when it denies class action remedies and compels individual arbitration of TILA claims).

Petitioner's invocation of *Gilmer v. Interstate/Johnson Lane Corp.*, 500, U.S. 20 (1991), is of no avail in this case because remedies in an individual plaintiff's Age Discrimination in Employment Act case, such as *Gilmer,* include recovery of unpaid wages, reinstatement, other equitable relief, liquidated damages for willful violations, plus attorney fees and costs. 29 U.S.C. §626(b) (incorporating remedies of 29 U.S.C. § 216). Individual employment discrimination claims thus are viable on their own, and it is comparing apples and oranges to apply *Gilmer's* analysis to Truth In Lending Act claims such as this one, where individual remedies are limited to $200 to $2,000, or actual damages (here $15), plus fees and costs. *See* 15 U.S.C. § 1640(a)(1) and (2)(A). Unlike the plaintiff in *Gilmer*, TILA claimants effectively lose their claims when they are denied their statutory right to proceed as a class.

This Court has held that congressional intent to override the Federal Arbitration Act's enforcement of contractual arbitration clauses must be deducible from the overriding statute's text or legislative history or from an "inherent conflict between arbitration and the statute's underlying purposes." *McMahon*, 482 U.S. at 226-27. The legislative history of the Truth In Lending Act's class action provisions, and the Act's underlying purpose to empower consumers to provide effective enforcement through civil actions, demonstrate that petitioner's attempt to subvert class action proceedings through mandatory individual arbitration is in irreconcilable conflict with TILA. Since petitioner is using its arbitration clause to compel individual arbitration, the clause is unenforceable as applied to respondent's Truth In Lending Act claim.

B. The claims of the proposed plaintiff class cannot be ordered to arbitration because arbitrators do not have authority to bind absent class members to their judgments.

Respondent filed this suit seeking certification of a nationwide class of home mortgage borrowers attempting to vindicate their claims under the Truth In Lending Act. Petitioner has invoked its arbitration clause to preclude respondent from resorting to TILA's class action remedies without addressing the question of whether the nationwide class could pursue its claims for class-wide relief in arbitration. The District Court answered this question in the negative after summarily concluding that class actions are merely procedural devices under TILA. *Randolph v. Green Tree Financial Corp.*, 991 F. Supp. 1410, 1423-24 (M.D. Ala. 1997). Respondent argues that the absence of an explicit class action provision in petitioner's arbitration clause precludes mandatory arbitration

of individual claims. We agree. But respondent also argues that, if there were such a provision, the TILA claims of a nationwide class could be resolved through mandatory arbitration. We disagree because an arbitral resolution of the claims of a plaintiff class cannot have preclusive effect on absent class members since arbitrators have no authority to bind absent parties.

This Court held in *Philips Petroleum Co. v. Shutts*, 472 U.S. 797 (1985), that an absent plaintiff class member's cause of action for money damages is a constitutionally protected property interest which entitles the absentee to due process guarantees before an adverse judgment of a court of law may permanently extinguish the claim through *res judicata*. *Id.* at 807, 811; *see also Hansberry v. Lee*, 311 U.S. 32, 42 (1940) ("there has been a failure of due process only in those cases where it cannot be said that the procedure adopted, fairly insures the protection of the interests of absent parties who are to be bound by it"); *Martin v. Wilks*, 490 U.S. 755, 761-62 (1989). Due process protections for absent plaintiff class members include the right to notice of the pending disposition of the cause of action, the opportunity to be heard and participate in the pending proceedings, the opportunity to opt out of the class, and the right to adequate representation by the named plaintiff at all times during the proceedings. *Shutts*, 472 U.S. at 812; *Ortiz v. Fibreboard Corp.*, 119 S. Ct. 2295, 2315 (1999). The determination as to whether, for example, the notice provided to absent class members was the best practicable to afford them the opportunity to present objections, *Mullane v. Central Hanover Bank and Trust Co.*, 339 U.S. 306, 314-15 (1950), or whether the named plaintiffs adequately represent the absent parties, *Hansberry*, 311 U.S. at 42-43, must be made by the state, which alone has constitutional authority to extinguish a claim of a non-party. Otherwise, a property right would be extinguished without due process.

An arbitrator's decision has no preclusive effect as to constitutional questions relating to the arbitration proceeding. In *McDonald v. City of West Branch*, 466 U.S. 284 (1984), this Court unanimously held that a federal court hearing a Section 1983 claim could not give preclusive effect to a prior arbitration award. *Id.* at 292. The plaintiff in *McDonald* first arbitrated and lost a wrongful discharge claim under a collective bargaining agreement, then asserted in his Section 1983 suit that his city government employer violated his First Amendment rights by firing him in retaliation for his engagement in protected speech and petitioning activity. *Id.* at 285-86. The *McDonald* Court held that the unappealed arbitration decision did not preclude the plaintiff from litigating his First Amendment claim because the Full Faith and Credit Act, 28 U.S.C.§ 1738, applies only to judicial proceedings, not to unappealed arbitration awards, and because judicial preclusion rules apply only to claims that are enforceable through courts, not private dispute resolution systems. *Id.* at 288-89. In so holding, the Court explained that:

> Although arbitration is well suited to resolving contractual disputes, our decisions in *Barrentine* and *Gardner-Denver* compel the conclusion that it cannot provide an adequate substitute for a judicial proceeding in protecting the federal statutory and constitutional rights that § 1983 is designed to safeguard. As a result, according preclusive effect to an arbitration award in a subsequent § 1983 action would undermine that statute's efficacy in protecting federal rights...
>
> ...An arbitrator may not, therefore, have the expertise required to resolve the complex legal questions that arise in § 1983 actions.

Id. at 290. The disposition of the legal claims of a nationwide class would necessarily involve due process determinations that similarly exceed the authority and competence of a private arbitrator.

Beyond the issue of an arbitrator's power to bind anyone who has not consented to the specific proceeding, it would be an enormous stretch to apply the Federal Arbitration Act to compel arbitration of a class action, especially in light of the Act's history discussed above. For example, the determination of whether absent plaintiffs' interests are adequately represented involves complex legal questions that an arbitrator presiding over a class action would have to decide. Adequate representation by named plaintiffs requires an alignment of interests between the named and absent parties, identification of conflicting interests within the class and separate representation of such interests, and an allocation of recovered resources that is responsive to the differing interests of any subclasses. *See Ortiz*, 527 U.S. at 854-58; *Amchem Products, Inc. v. Windsor*, 521 U.S. 591, 626-27 (1997); *In re General Motors Corp. Pick-Up Truck Fuel Tank*, 55 F.3d 768, 801 (3d Cir. 1995). The arbitrator would also have to ensure that absent class members have been adequately represented by counsel. This would require the arbitrator to examine the timing and terms of any disposition, differentiate counsel's interest in maximizing hourly fees from the party's interest in a just recovery, and search for evidence of collusion between defendants and plaintiffs' counsel against the interests of some or all of the class. *Id.* at 802-03. Such complex legal determinations, which are grounded in due process standards, not the law of the marketplace, far exceed the competency and authority of private arbitrators and bear no resemblance to the kind of business to business arbitration that those who drafted the FAA envisioned.

Finally, arbitral resolutions of these complex legal questions pertaining to the rights of absent class members would almost certainly be beyond review of any court. In contrast to the searching appellate review which *Amchem* and *Ortiz* illustrate to have been so vital in protecting absent class members from the pressures that named parties may exert on decision-makers, judicial review of the merits of arbitral determinations under Section 10 of the FAA is exceedingly deferential and would necessarily sacrifice this protection. *See, e.g., First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 942 (1995) (court will set aside merits of arbitrable decisions "only in very unusual circumstances" such as fraud, corruption, or manifest disregard of the law); *Halligan v. Piper Jaffray, Inc.*, 148 F.3d 197, 202 (2d Cir. 1998) (to modify an arbitral award on the merits, court must find that "(1) the arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether, and (2) the law ignored by the arbitrators was well defined, explicit, and clearly applicable to the case"). The FAA's failure to provide meaningful judicial review of arbitral determinations further shows why the Act was never intended to apply to class-based claims.

In attempting to compel individual arbitration under the Federal Arbitration Act, petitioner is effectively preventing consumers from enforcing the Truth In Lending Act's class action remedies for serial violations. To allow compelled arbitration in this situation would sever application of the FAA from the congressional purposes and policy goals that underpinned its enactment. The use of mandatory arbitration to preclude the award of class-wide relief would undermine the TILA's civil enforcement scheme by abrogating the Act's strongest deterrent penalty. Even if the parties attempted to arbitrate the claims of a TILA class, the proceeding would exceed the authority and competency of private arbitral decision-making far beyond anything ever contemplated, much

less ratified, by Congress in the Federal Arbitration Act, or permitted by the Due Process Clause as applied to absent class members.

CONCLUSION

The decision of the court of appeals declaring petitioner's arbitration clause unenforceable should be affirmed.

Respectfully submitted,

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